Before The
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992	)	MM Docket No. 92-266
	)	
	)	
Rate Regulation	)	

REPLY COMMENTS OF
AFFILIATED REGIONAL COMMUNICATIONS, LTD.

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I. Commercial Rate Regulation.

Every commenter addressing the issue opposed regulation of commercial cable rates. The 1992 Cable Act does not require the Commission to regulate those rates and the Commission has gathered no information which might provide a reasonable basis for such regulation. Moreover, fundamental differences between residential and commercial customers justify different and higher rates for commercial establishments. Unlike residential subscribers, commercial establishments use cable services to attract customers and increase their own revenues. They also allow large numbers of people to view cable programming without paying the cable operator or the programmers.

Other audio and video programming distribution and/or licensing arrangements identified by the parties charge commercial establishments higher rates than residential customers. In particular, the record indicates that competitive cable systems differentiate between residential and commercial customers, and the Commission recently found "no basis to question" the National Football League's rate structure for its satellite "season ticket" package, which requires commercial establishments to pay up to 25 times more for that service than residential subscribers.

II. Going-Forward Rules.

Virtually every programmer reported that the growth of existing program networks and the launch of new services have been stalled by rate regulation and the inadequate incentives provided under the current going-forward rules. A flat fee increase of

between 25 and 40 cents plus the programming cost for each new service added will better facilitate expansion of regulated service offerings. However, this approach will not completely eliminate regulatory bias from carriage decisions because the flat fee will provide the cable operator a lower margin on higher-cost services.

If the Commission determines that an annual cap on rate increases resulting from the addition of new programming services is necessary, it should structure the cap to exclude the cost of new programming in order to avoid skewing carriage decisions against local and regional programming. The Commission has recognized that such services provide substantial public interest benefits but tend to be more costly because their programming is more expensive to produce and appeals to cable subscribers in limited geographic areas. In the alternative, the Commission should exclude from the cap the cost of local and regional programming services in order to promote the Congressional objectives of diversity and local origination of programming.

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Affiliated Regional Communications, Ltd. ("ARC") submits these Reply Comments in response to selected comments in this proceeding. The record confirms that regulation of commercial rates is unnecessary and unwarranted, and that significant differences between residential and commercial cable customers support higher rates for commercial customers. Although the current "going-forward" rules should be modified to enable cable operators to expand regulated service offerings, adoption of an annual cap on resulting rate increases which includes the cost of new local and regional programming services would unreasonably discriminate against future carriage of such services on regulated tiers, undermining the Congressional objectives of diversity and localism.

Introduction

In its Fifth Notice of Proposed Rulemaking,[1] the Commission sought further comment on whether "we should establish regulations governing rates for regulated cable service provided to commercial establishments." Fifth Notice at ¶257. In its initial comments, ARC opposed any regulation of commercial cable rates and demonstrated that there are fundamental differences between residential and commercial cable service which preclude a uniform rate structure for those customers. Commenters uniformly opposed commercial rate regulation and confirmed that such regulation is unwarranted.

The Fifth Notice also sought further comment on whether the Commission's "going-forward methodology should be modified to provide greater or lesser compensation to operators for adjustments to capped rates when channels are added or deleted from regulated tiers." Fifth Notice at ¶256. Commenters agreed that a reasonable "flat fee" rate increase would provide a greater incentive for cable operators to add new program services to regulated tiers and promote "neutrality" in carriage decisions between low and high cost services. However, certain proposals to establish annual caps on rate increases, and to include the cost of new programming services

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[1] Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking, MM Docket No. 92-266, FCC 94-38 (rel. Mar. 30, 1994) ("Fifth Notice").

under such caps, would create a substantial disincentive to adding local and regional programming services.

I. The Commission Should Not Regulate Commercial Rates.

In its initial comments, ARC -- and every other commenter addressing the issue -- opposed regulation of commercial cable rates. The record developed in response to the Fifth Notice demonstrates that there is no reasonable basis for regulation of commercial cable rates, much less any requirement that they be equivalent to, or somehow used to subsidize, residential rates.

A. Differences Between Commercial And Residential Customers Justify Higher Rates For Commercial Establishments.

As set forth in its initial comments, ARC's regional cable sports programming services traditionally have differentiated between residential and commercial customers receiving its programming services. Regardless of the distribution technology involved, ARC's license fees for distribution of its programming services to commercial establishments are not based on its fees for residential distribution, but rather on the "Estimated Viewing Area" of each commercial establishment.[2] See ARC Comments at 4. Other parties have confirmed

[2] Generally, ARC charges higher license fees to distributors, which in turn charge each commercial customer. In the alternative, ARC's regional services may enter into licensing agreements directly with commercial establishments desiring to receive ARC's programming. In such cases, the

that differences between residential and commercial customers justify this historical distinction in services and rates.

1. Higher License Fees And Rights Payments

First, cable operators in some instances charge higher rates to commercial customers because certain programmers -- including ARC's regional sports services -- charge cable operators higher license fees when they distribute the programming to commercial establishments. In turn, ARC's regional sports services generally are required to pay higher rights fees to professional sports teams in return for the right to distribute their games to commercial establishments. Thus, the professional sports teams which license ARC's regional networks to carry their games "have a vital financial interest" in the preservation of the current rate structure for commercial establishments. NHL Comments at 8.

As ARC discussed in its initial comments, the professional sports teams have a significant interest in protecting the "gate" for home games, which in most cases constitute the majority of games licensed to regional sports networks. ARC Comments at 5; see also NHL Comments at 9

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commercial establishment pays a license fee directly to the regional sports network, and the network pays the cable operator a fee to deliver the signal to each establishment. Comments of the National Hockey League ("NHL") at 8 n.19 ("[o]n occasion, the RSN [regional sports network] will itself perform the marketing and sales function to the commercial establishment").

("sports teams have a traditional and legitimate concern that showing home games on television may reduce revenues from ticket sales").[3] Allowing large numbers of fans to view home games at sports bars and restaurants rather than the ballpark adversely affects the gate receipts for those events. To compensate for the lost revenues, teams typically have sought either a share of the higher rates charged by regional sports networks to commercial establishments or a higher general rights fee in return for allowing the team's games to be distributed to such establishments. See NHL Comments at 9 (The adverse "financial impact" on the team of allowing "potentially thousands of customers" to gather "in venues of significant size which replicate the arena situation...is alleviated by the premium paid to the team by the RSN [regional sports network] for the rights to license these bars and restaurants"). Absent the ability to recover such premium payments, "teams may seek to offset their losses by increasing

[3] The Commission has recognized that professional sports teams attempt to protect the gate for home games by licensing broadcast stations to carry away games while regional cable sports services generally carry the home games. See Final Report, PP Docket No. 93-21, FCC 94-149 (rel. June 30, 1994) ("Final Sports Migration Report") at ¶159 ("broadcast coverage is overwhelmingly of away games and...cable coverage is primarily of home games"). The Commission noted that it appears that "teams prefer to license home games to cable networks, because they feel that the need to subscribe to cable provides some protection to the live gate or that cable rights fees provide some compensation for any decline in attendance caused by cable viewing." Id. at ¶158.

attendance revenues through a reduction in the number of televised home games, a rise in ticket prices or both." Id.

2. Commercial Value Of Cable Programming

ARC also charges higher rates to commercial establishments because unlike residential subscribers, commercial customers use ARC's programming to attract customers and increase their own revenues. ARC Comments at 5-6. The same rationale justifies higher cable rates for commercial establishments. See Comments of Time Warner Cable ("Time Warner") at 34 (commercial customers "are primarily concerned with attracting additional business by offering cable service to their customers"); Comments of Rainbow Programming Holdings, Inc. ("Rainbow") at 4 ("when a bar owner shows his customers a New York Mets game licensed to SportsChannel, he is effectively giving that game away to scores of patrons in order to increase his revenues from the sale of food and beverages"). Consequently, commercial establishments derive substantial additional value from ARC's programming and other cable services as compared to residential subscribers. See, e.g., Comments of Cablevision Systems Corporation ("Cablevision Systems") at 6 n.10 (bar owner indicated that ability to offer televised Boston Red Sox baseball game can increase bar revenues by $200 to $300 per night).

In fact, commercial establishments often advertise the availability of cable to attract customers. See Comments

of Pagosa Vision, Inc. at 3 ("[t]he casino and casino/hotel use cable television to attract gambling tourists"); NHL Comments at 6 ("taverns have found that they can significantly increase their patronage and their food and drinks sales by offering a range of sports events on television"). Thus, cable "clearly provides an economic value to the commercial user many times that which is conferred upon a residential subscriber." Time Warner Comments at 35. Consequently, it is reasonable to require commercial customers to compensate the cable operator (and the programmer) "for the additional value that its sports programming creates for commercial establishments." Rainbow Comments at 3.

3. Compensation For Lost Revenues

ARC also charges more for distribution of its programming to commercial establishments because those establishments allow large numbers of individuals to view those services and ARC has no other way to receive compensation from those individuals. ARC Comments at 6. For example, sports bars and restaurants subscribing to ARC's services may range from small neighborhood taverns to huge establishments capable of seating hundreds of people. See NHL Comments at 5-6 ("sports bars are not necessarily 'Mom-and-Pop' operations," and instead may have 30 or more televisions serving over 600 people). Again, the same rationale applies to other cable services. Patrons of these establishments "may forego

subscribing to a sports programming service -- or subscribing to cable altogether -- because they can view the games exhibited by that service" in the company of other fans at the local sports bar, resulting in lost revenues to the programmer and the cable operator. Rainbow Comments at 5. Such revenues can be recovered only through higher rates charged to the commercial establishment. See Cablevision Systems Comments at 6-7.

4. Consistency With Other Commercial Licensing Arrangements

Other programming distributors and licensing arrangements recognize these differences between residential and commercial customers and charge higher rates to commercial customers. ARC Comments at 7-10. In addition to the NFL and ESPN satellite packages described in ARC's Comments at 7-8,[4] numerous other video and/or music distribution and licensing

[4] The NFL proposes to charge residential home satellite dish subscribers between $100 and $140 for its "season ticket" package of out-of-market games and commercial subscribers between $700 and $2,500 for the same package, depending on the size of each establishment. See Final Sports Migration Report at ¶168. Since ARC's initial comments were filed, the Commission has reviewed the NFL's commercial rate package in the context of its sports migration inquiry. The National Licensed Beverage Association filed comments in that proceeding objecting to the higher rates charged by the NFL and advocating "a new compulsory license for sports bar carriage of sports programming." Id. at ¶166. However, the Commission concluded that the NFL satellite package "appears to be a net addition to output and to the choices lawfully available to dish owners and commercial establishments." Significantly, the Commission stated that it had "no basis to question the announced price structure of the package." Id. at ¶171.

arrangements charge higher rates to commercial customers. For example, the license fees established by the American Society of Composers, Authors and Publishers and Broadcast Music, Inc. are based on the seating capacity of commercial establishments. See Comments of Tele-Communications, Inc. ("TCI") at 34. "[P]ay-per-view and cable music companies as well as ...DBS companies" follow a similar model and charge higher rates to commercial establishments. See Comments of Continental, Cablevision, Inc. and KBLCOM, Inc. ("Continental/KBLCOM") at 9-10 and Exhibits 3 through 6. Finally, a survey of competitive cable systems submitted by TCI indicates that those systems also charge different rates for residential and commercial customers. See TCI Comments at 36-37; S. Besen and J. Woodbury, "Results of a Survey of Commercial Rates Charged By Overbuilt Cable Systems" (June 29, 1994).

B. There Is No Basis For Regulation Of Commercial Rates In Any Event.

The differences between commercial and residential customers described above clearly demonstrate that regulations requiring equivalent rates would be arbitrary and capricious. More importantly, the record provides no reasonable basis for regulating commercial cable rates at all.

1. No Statutory Requirement To Regulate Commercial Rates

The Commission stated that it was "not persuaded" to authorize different and "presumably higher" cable rates for

commercial establishments because neither the Cable Television Consumer Protection and Competition Act of 1992 ("1992 Cable Act") nor its legislative history "evince an intent" that commercial establishments should pay higher rates." Fifth Notice at ¶185. However, neither the 1992 Cable Act nor the legislative history mentions commercial rates; each makes clear that Congress was concerned solely with protecting residential subscribers.

The 1992 Cable Act requires the Commission to develop regulations regarding the rates charged to cable "subscribers." 47 U.S.C. §543(b)(2). The Commission defines "subscriber" as a "member of the general public who receives broadcast programming distributed by a cable television system and does not further distribute it." 47 C.F.R. §76.5(ee). Because commercial establishments effectively "distribute" programming to their customers, they clearly are not within the category of "subscribers" which Congress sought to protect. See TCI Comments at 33-34; Continental/KBLCOM Comments at 1-2.

Likewise, the legislative history makes no mention of commercial rates. Continental/KBLCOM Comments at 2. Instead, by repeatedly referring to "households," "private homes," "dwelling units" and "cable homes," the legislative history clearly establishes that Congress focused on the regulation of residential cable rates. Id. at 2-3; TCI Comments at 35-36; Cablevision Systems Comments at 3-5.

Finally, the Commission has determined that the rate regulation provisions of the 1992 Cable Act do "not prohibit the establishment by cable operators of reasonable categories of service and customers with separate rates and terms and conditions of service, within a franchise area." 47 C.F.R. §76.984(b). As set forth above, the differences between residential and commercial cable customers clearly warrant "separate rates and terms and conditions of service."

2. No Determination Of Lack Of Effective Competition

There is no basis for commercial rate regulation because there is no evidence of the absence of effective competition to cable among commercial customers. Instead, the evidence indicates that commercial customers in most cases have readily available alternatives to cable service. ARC Comments at 12. Cable operators reported that they face substantial competition from alternative distribution technologies in seeking to serve commercial establishments. See Continental/KBLCOM Comments at 10-11 (35 percent of bars in Continental's Western New England service area subscribe to SMATV; 60 percent of bars in Jacksonville, Florida service area subscribe to SMATV; "SMATV and PPV providers such as Spectradyne" serve 60 percent of hotels and motels); Comments of Cablevision Industries Corporation ("CVI") at 20-21 (CVI "is almost always met by competition from numerous satellite companies, including Spectradyne, Comsat, On Command Video,

Lodgenet, World Cinema and Wireless Cable Companies" in seeking to serve hotels and motels; bar owners frequently purchase satellite dishes rather than subscribe to cable); Cablevision Systems Comments at 4 (20 percent of bars in its Connecticut service area "use satellite dishes rather than subscribe to cable" and 17 percent of bars in its Boston service area do the same).

The availability of these alternatives has had a significant effect on cable penetration among commercial establishments. Cable operators have indicated that penetration rates for commercial establishments are substantially lower than residential penetration rates. See Time Warner Comments at 39 (commercial cable penetration in Manhattan, Queens and Brooklyn is less than 4 percent). If the Commission does not consider commercial establishments separately, then it must reconsider the presence of effective competition for purposes of overall rate regulation.[5] See Time Warner Comments at 32 ("if commercial establishments are deemed 'households' subject to potential [rate] regulation, then all commercial establishments would have to be counted as house-

[5] Inclusion of commercial revenues also would require re-calculation of overall benchmark rates. See Continental/KBLCOM Comments at 15 ("inclusion of higher commercial rates would cause the regulated revenues per subscriber as of September 30, 1992 to increase, thereby raising the absolute level of an operator's full reduction rate").

holds in order to determine whether the affected cable systems were subject to effective competition").

3. No Record Support For Regulation

In any event, the Commission simply does not have the information necessary to regulate commercial rates in a reasonable manner. The data gathered by the Commission in order to establish benchmark residential rates did not include any information regarding commercial cable penetration, revenues, or rates. See, e.g., TCI Comments at 40 ("the exclusion of commercial rates from its surveys highlights the fact that the Commission has no basis to regulate commercial rates because it has no information on which to do so") (emphasis in original). Absent such record evidence, adoption of commercial cable rate regulations would be arbitrary and capricious. See Turner Broadcasting Co. v. F.C.C., 62 U.S.L.W. 4647, 4659 (June 27, 1994) (citing "paucity of evidence" supporting must-carry provisions); Home Box Office Inc. v. F.C.C., 567 F.2d 9, 40 (D.C. Cir.), cert. denied, 434 U.S. 829 (1977) ("Whatever may be the ultimate validity" of the Commission's rationale for anti-siphoning rules, the "principal defect on...review is that there is no record evidence to support it"). In this case, Congress did not require such regulation and no commenter in this proceeding has even suggested that commercial rate regulation is necessary.

II. Annual Caps Which Include Programming Costs Will Unreasonably Deter Carriage Of Local And Regional Programming.

ARC supports the proposal, advanced by nearly all commenters, to adopt a reasonable "flat fee" mark-up for each new channel added to a regulated service tier.[6] Whether adopted as an alternative to a percentage mark-up on programming costs,[7] or a substitute for such mark-up, a reasonable flat fee increase will offer greater incentives than the current rules for carriage of new programming services and will restore some degree of neutrality to carriage decisions between high and low cost services. However, the flat fee approach will not eliminate cost-based discrimination in carriage decisions. By yielding a lower margin on higher-cost services, a "flat fee" mark-up discriminates to some extent against higher-cost programming services. Moreover, ARC opposes the imposition of any annual cap on rate increases resulting from the addition of new services if the cap

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[6] Commenters generally argued for a flat fee in the range of 25 to 40 cents per channel, plus the cost of the programming. See TCI Comments at 24 (25 cents); Comments of USA Network ("USA") at 9-10 (25 cents plus a 5 cent "adjustment factor"); CVI Comments at 14 (35 to 40 cents). See also Comments of the Cable Telecommunications Association at 4-5 (sliding scale of 25 cents to 50 cents depending on system size).

[7] Some commenters argued that the percentage mark-up should be retained as an alternative, but the percentage should be increased. See Comments of Providence Journal Corp. ("Providence") at 6 (cable operator choice between "improved percentage mark-up" and "flat fee"); Time Warner Comments at 6 (25 cents or 25 percent of program costs, whichever is greater).

includes the new programming costs because such caps unreasonably will discriminate against local and regional news and sports services, undermining important objectives of the 1992 Cable Act.

A. Appropriate Incentives Should Promote Diversity And Local Origination Of Programming.

The record in this proceeding clearly confirms that the Commission's current "going-forward" rules are not working. See, e.g., Comments of Court TV at 11 (since rate regulations became effective "growth of Court TV has all but stopped"); USA Comments at 2 (since adoption of rate regulations, "there has been a virtual 'freeze' on the growth of fledgling services and the launch of new services"); Comments of E! Entertainment Television, Inc. ("E!") at 2 ("launches of E! by new affiliates have reached a standstill" since rate regulations were implemented); Comments of Jones Education Networks at 2 ("the steady growth in our subscribership [to Mind Extension University] has stalled...[as] the result of the Commission's rate regulation").

The current rules simply provide inadequate incentive for cable operators to add new services to regulated tiers and may discriminate against addition of low-cost services. See, e.g., Comments of Turner Broadcasting System, Inc. at 1 ("without additional, more adequate incentives, the availability and quality of programming will be adversely

affected"); Providence Comments at 4 (the "current cost plus percentage approach" creates "an imbalanced playing field and thereby disadvantages low cost and no cost programming" services); Comments of Lifetime Television ("Lifetime") at 7 ("the current going-forward rules create the greatest barriers to broad tier carriage for cable networks with the lowest license fees") (emphasis in original).

However, in seeking to remedy these problems, the Commission should avoid rules which may bias carriage decisions against local and regional news and sports services which contribute substantially to diversity and localism -- two clearly articulated Congressional goals. 1992 Cable Act, §§2(a)(10), 2(b)(1). The Courts and the Commission repeatedly have recognized that live coverage of "outstanding local events [such] as community concerts, civic meetings, local sports events, and other programs of local consumer and social interest" serves the public interest. United States v. Midwest Video Corp., 406 U.S.649, 668-69 (1972), quoting National Broadcasting Co. v. United States, 319 U.S. 190, 203 (1943) (emphasis added). See also Second Report and Order, MM Docket No. 92-264, 8 FCC Rcd. 8565 (1993), at ¶78 (local and regional programming services are "responsive to the needs and tastes of local audiences and serve[s] Congress' objectives of promoting localism").

At the same time, the Commission has recognized that such "local and regional programming services are usually

costly to produce and appeal only to a limited population of subscribers" as compared to other programming services. Id. Because local and regional programming services are more expensive to produce and are distributed to limited numbers of subscribers, they have higher license fees than other programming services which offer little or no live programming and are distributed nationally. Consequently, these services are likely to be seriously and adversely affected by regulations which skew carriage decisions against higher-cost services.

B. Any Annual Cap On Rate Increases Resulting From Addition Of New Services Should Be Formulated To Exclude New Programming Costs.

Several commenters have suggested that if the Commission adopts a flat fee mark-up for new programming services, it would be reasonable to adopt an "annual cap of $1.50 on the amount of license fees and flat fees that an operator could pass through" as a result of adding new services to regulated tiers. Comments of Discovery Communications, Inc. ("Discovery") at 8; see also CVI Comments at 14 ("it would be reasonable to limit such increases to $1.50 annually (which amount would include the programming license fee and the fixed pass-through)"). ARC respectfully suggests that by including the cost of the new programming under the cap, these proposals would affirmatively discourage future carriage of local and regional programming services, undermining the Congressional objectives and public interest benefits described above.

For example, the rights fees and other costs of one of ARC's regional sports networks which televises games involving several different professional sports teams necessitate charges to cable operators within the network's "inner market" of $1.00 per subscriber per month. Inclusion of that cost, plus a flat fee mark-up within the range suggested by the parties in this proceeding, would virtually exhaust the $1.50 annual cap proposed by Discovery and CVI. Cable operators likely will be unwilling to add local and regional services where such addition would eliminate or severely restrict their flexibility to add other services for the remainder of the year.

To avoid skewing carriage decisions against higher-cost services, ARC respectfully suggests that all new programming costs be excluded from any annual cap adopted by the Commission on rate increases resulting from the addition of new programming services. See Lifetime Comments at 15 ("The Commission has long made clear that all programming costs should be fully recovered on an external basis, and no cap should be allowed to frustrate this fundamental tenet"). Clearly, adoption of a flat fee increase rather than a percentage mark-up would eliminate any artificial incentive to add higher-cost services, such as regional sports services, to regulated tiers. Indeed, a flat fee mark-up on higher-cost programming services is likely to reduce the cable operator's overall margin, creating a disincentive to add such services.

Consequently, cable operators will add those services only if they perceive a substantial demand on behalf of their subscribers. There simply is no reason to prejudice carriage decisions against local and regional services by including the cost of those services in any annual cap on rate increases.

Conclusion

Commercial cable rates should not be regulated by the Commission, and in no event should the Commission mandate equivalent commercial and residential rates or residential rate subsidies. An appropriate "flat fee" increase would provide greater incentives for cable operators to add new services to regulated tiers, but including the cost of those services in any annual cap on rate increases would unreasonably discriminate against carriage of local and regional programming services.

Respectfully submitted,

July 29, 1994

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